FILED

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No. OFFICE OF THE CLERK

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1995

ARIZONA CENTRAL RAILROAD,

Petitioner,

v.

STATE OF ARIZONA; ARIZONA DEPARTMENT OF REVENUE; CITY OF PHOENIX; AND TOWN OF CLIFTON,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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50 pp

QUESTION PRESENTED

Does Arizona's imposition of state excise taxes on rail carriers but not on motor carriers, the rail carriers' principal competitor, discriminate against rail carriers in violation of the 4-R Act, which was enacted by Congress for the specific purpose of ensuring that state taxes do not place rail carriers at a competitive disadvantage vis-a-vis other carriers of freight and passengers?

LIST OF ALL PARTIES BELOW

The Atchison, Topeka and Santa Fe Railway Company
Southern Pacific Transportation Company
Arizona Central Railroad
State of Arizona
Arizona Department of Revenue
City of Phoenix
Town of Clifton

RULE 29.6 STATEMENT

Pursuant to Rule 29.6, Petitioner Arizona Central Railroad discloses that it has no parent company, subsidiary or affiliate that has issued shares of stock to the public.

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OPINION BELOW

The Atchison, Topeka and Santa Fe Railway Company v. The State of Arizona, 78 F.3d 438 (9th Cir. 1996). The District Court opinion contained in the Appendix is unpublished.

BASIS FOR JURISDICTION

The judgment of the United States Court of Appeals for the Ninth Circuit was entered March 4, 1996. A timely filed petition for rehearing was denied May 6, 1996. Jurisdiction is conferred by 28 U.S.C. § 1254.

STATUTES INVOLVED

49 U.S.C. § 11503 (originally enacted as The Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act"), § 306).[1] Railroads are subject to Arizona state taxes, A.R.S. §§ 42-1310.02, 1408. Motor carriers are exempt from these taxes, A.R.S. §§ 42-1310.02, 1409(a)(5). *See* Appendix.

STATEMENT OF THE CASE

Factual Background

Petitioner Arizona Central Railroad ("Arizona Central") operates a rail line entirely within Arizona. The Atchison, Topeka, and Santa Fe Railroad ("Santa Fe") and Southern Pacific Railroad ("Southern Pacific") own and operate railroads located, in part, in Arizona. The railroads pay Arizona state and local transaction privilege taxes on "the business of transporting for hire persons, freight or property by motor vehicle, railroads or aircraft from one point to another point in this state." A.R.S. § 42-1310.02(a). The state tax is calculated at five percent of the gross proceeds or gross income derived from the railroads' intrastate business activity within Arizona. Railroads also pay Arizona state

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[1] In 1995, § 11503 was renumbered to § 11501. Pub.L. 104-88, Title I, § 102(a), Dec. 29, 1995, 109 Stat. 843.

and local use tax on out-of-state purchases of diesel fuel to power locomotives. A.R.S. § 42-1408.

Tax revenues paid by the railroads go to the general fund of the state (or city) and are not used for the construction or maintenance of railroad tracks. Railroads build and maintain their own tracks.

Motor carriers are exempt from the transaction privilege tax or any similar tax imposed by any taxing authority within Arizona on their transportation activity. A.R.S. § 42-1310.02(A)(1). Diesel fuel purchased out of state by motor carriers for transportation on public roads is exempt from the use tax. A.R.S. § 42-1409(a)(5).[2]

Motor carriers are taxed under a separate tax system (codified in Title 49 of the Arizona Revised Statutes) that includes a motor carrier tax (based on the weight of the vehicle and the number of miles driven in the state) and a use fuel tax. Revenues from the motor carrier tax and the use fuel tax are constitutionally earmarked for expenditure for "highway and street purposes." Arizona Constitution, Art. 9, § 14. Unlike railroads, therefore, motor carriers are taxed under a scheme designed to impose on those carriers the approximate maintenance cost they impose on the highway system. Motor carriers do not otherwise pay for the use or maintenance of the highways. According to studies sponsored by Arizona, heavy commercial trucks have historically paid to the state less than the full cost of highway maintenance and construction resulting from the motor carriers' use of the roads.

In Arizona, heavy freight is transported primarily by railroads and motor carriers. In comparing the cost of shipping goods, shippers of freight must include in their comparison the transaction privilege tax if they ship by rail, but not if they ship by motor carrier. Thus, the imposition of the transaction privilege tax on rail carriers but not on motor carriers is a significant competitive disadvantage for rail carriers. Railroads do not compete for transportation of heavy freight with the other

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[2] On the local level, the railroads are similarly taxed, while motor carriers are exempt. Model City Tax Code §§ 475, 610, 475(D)(1), 660(j).

businesses subject to the Arizona transaction privilege tax on transportation.

Jurisdiction and Procedural History

Santa Fe and Southern Pacific, together with Petitioner, filed suit in the United States District Court for the District of Arizona under 49 U.S.C. § 11503(c) and 18 U.S.C. § 2201, *et seq*. The railroads sought declaratory and injunctive relief against the imposition on them of: (1) Arizona state and local transaction privilege taxes imposed on "the business of transporting for hire persons, freight or property by motor vehicle, railroads or aircraft from one point to another point in this state"; and (2) Arizona state and local use tax railroads pay principally on out-of-state purchases of diesel fuel.

Following cross-motions for summary judgment, the District Court entered judgment for the railroads, holding that the Arizona tax scheme discriminated against rail carriers in violation of the 4-R Act. The defendant tax authorities (the State of Arizona, the City of Phoenix and the Town of Clifton) appealed, and the Ninth Circuit reversed and remanded with directions to enter judgment in favor of the defendants. A petition for rehearing was denied.

Summary of Reasons for Granting the Petition

Petitioner Arizona Central is a rail carrier transporting freight and passengers entirely within the State of Arizona. Other railroads also transport freight in the State of Arizona and surrounding states. During the fiscal year ending June 30, 1992, alone, the railroads operating in the State of Arizona remitted to the State over $2 million in transaction privilege and use taxes (IR 62, ¶¶ 2, 17). Motor carriers, the railroads' principal competitors, do not pay these taxes. This disparate treatment constitutes discrimination. The resulting competitive disadvantage must be redressed under the 4-R Act, which was enacted by Congress specifically to prohibit such discrimination.

By reversing (over a vigorous dissent) the summary judgment granted in the District Court, the United States Court of Appeals for the Ninth Circuit became the first federal or state court to uphold, against a 4-R Act challenge, the imposition of

taxes upon railroads that are not also applied to motor carriers. The Ninth Circuit's decision creates a conflict with the highest courts of two states which, under similar circumstances, have held that taxes that apply to rail carriers but not their principal competitors discriminate against the railroads in violation of the 4-R Act. Burlington Northern Railroad v. Commissioner of Revenue, 509 N.W.2d 551 (Minn. 1993); Atchison, Topeka and Santa Fe Railway v. Bair, 338 N.W.2d 338 (Iowa 1983), cert. denied, 465 U.S. 1071 (1984).

Further, the Ninth Circuit misread this Court's opinion in Department of Revenue v. ACF Industries, Inc, 510 U.S. 332, 114 S. Ct. 843 (1994). In that case, this Court held that states may "grant exemptions from a generally applicable ad valorem property tax" without violating the 4-R Act. 510 U.S. at ___, 114 S. Ct. at 846, 848, 852. The majority opinion below misapplied this Court's ACF Industries holding to validate the imposition of a nonproperty tax scheme which exempts the railroad's principal competitors. In holding that the railroads were treated fairly in comparison to other commercial and industrial taxpayers, the Court of Appeals for the Ninth Circuit ignored the "patently discriminatory effects" of the Arizona tax scheme. Finally, as evidenced by the Amicus Curiae briefs filed on behalf of five states in the Ninth Circuit, these issues have substantial importance beyond this particular litigation.

REASONS FOR GRANTING CERTIORARI

I. THE DECISION OF THE NINTH CIRCUIT CONFLICTS WITH DECISIONS BY TWO STATE COURTS OF LAST RESORT ON AN IMPORTANT QUESTION OF FEDERAL LAW.

A. Discrimination Under the 4-R Act is an Important Federal Question.

The purpose of the 4-R Act is to revitalize the railroad industry by making it competitive with other carriers of freight and passengers. Burlington Northern Railroad v. Commissioner of Revenue, 509 N.W.2d 551, 553 (Minn. 1993); Burlington

Northern Railroad v. Triplett, 682 F.Supp. 443, 446 (D. Minn. 1988). Congress intentionally defined Section 306(1)(d) in broad terms "to prevent tax discrimination against railroads in any form whatsoever." Ogilvie v. State Board of Equalization, 657 F.2d 204, 210 (8th Cir.), cert. denied, 454 U.S. 1086 (1981). The Ninth Circuit decision in this case ignores the anticompetitive and discriminatory effects of imposing state and local transaction and use taxes against railroads but not motor carriers.

The 4-R Act is important federal legislation which has been the subject of two opinions of this Court. Department of Revenue v. ACF Industries, Inc, 510 U.S. 332, 114 S. Ct. 843 (1994); Burlington Northern Railroad Co. v. Oklahoma Tax Comm'n, 481 U.S. 454, 107 S. Ct. 1855 (1987). Both of these opinions dealt with the application of the 4-R Act to state or local property taxes. This case involves the provision of the 4-R Act applicable to nonproperty taxes. Five states filed amicus curiae briefs in the Ninth Circuit, indicating the importance of this issue to the taxing authorities in the individual states. The highest courts of Iowa and Minnesota have reached precisely the opposite conclusion on the question presented by this case than that reached by the Ninth Circuit.

B. The Decision Conflicts With Two State Supreme Court Decisions.

Section 306 of the 4-R Act prohibits the states and their political subdivisions from enacting tax schemes that discriminate against railroads. Section 306(1) contains four subsections. Subsections (a), (b) and (c) limit discriminatory assessment ratios or tax rates in the taxation of railroad property. Subsection (d), on the other hand, forbids "the imposition of any other tax which results in discriminatory treatment of a common carrier by railroad . . ."[3] The legality of the transaction privilege and use

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[3] Section 306(1), adopted in 1976, was recodified as part of the Interstate Commerce Act in 1978. As codified at 49 U.S.C. §11503(b)(4), a state cannot "impose another tax that discriminates against a rail carrier . . ." The change in language "may not be construed as making a substantive change in the laws

taxes at issue in this case must be determined by application of subsection (d).[4]

The concept of discrimination implies comparison. Indeed, the basic conflict between the decisions in the Iowa and Minnesota Supreme Courts and the decision of the Ninth Circuit is over the appropriate comparison class to be used in a subsection (d) case. Section 306 specifies "commercial and industrial property" as the comparison class for subsections (a)-(c). Subsection (d), however, does not specify any comparison class to be used in determining whether a state's nonproperty tax is discriminatory.[5]

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replaced." Burlington Northern Railroad v. Oklahoma Tax Comm'n, 481 U.S. at 457 n.1, 107 S.Ct. at 1858 n.1. For that reason, the courts have held that it is appropriate to use the original language of section 306 rather than the recodified language in analyzing the statute. Richmond, Fredericksburg and Potomac Railway v. Department of Transportation, 762 F.2d 375, 377 (4th Cir. 1985); Atchison Topeka and Santa Fe Railway v. Bair, 338 N.W.2d 338, 343 (Iowa 1983), *cert. denied*, 465 U.S. 1071 (1984).

[4] The Ninth Circuit decision properly rejected Respondents' argument that § 306(1)(d) only applies to taxes imposed "in lieu" of discriminatory property taxes, noting that such interpretation "has been rejected by many Circuits." Atchison, Topeka & Santa Fe Railway, 78 F.3d at 441. Thus § 306(1)(d) prohibits "all discriminatory state taxes." *Id.*

[5] In a portion of the ACF Industries opinion which was not reversed by this Court, the Ninth Circuit reached a conclusion wholly at odds with its decision in this case. There the Ninth Circuit held that subsection (d) was not limited to the commercial and industrial comparison class.

> Section 306(1)(a) through (c) . . . restrict the comparison class to "other commercial and industrial property." There is no analogous restriction in the broad language of section 306(1)(d).

In this case, the Ninth Circuit incorrectly held that:

> the proper comparison class for determining whether the Arizona transaction privilege tax and use tax violate subsection (b)(4) of the 4-R Act is "all industrial and commercial taxpayers who are subject to the tax."

78 F.3d at 441-42.

The longstanding interpretation of the 4-R Act, established by the highest courts of Iowa and Minnesota, is directly contrary to the holding of the Ninth Circuit. In striking down a state tax on fuel, the Supreme Court of Iowa held:

> We thus approach the central question regarding section 11503: does the Iowa excise tax discriminate against railroads? The first problem involved in that question is this: with what other taxpayers and taxes do we compare the railroad fuel tax?
>
> Because individuals and corporations in business usually have property in their enterprises, a tax on railroad property is compared with state taxes on property of commercial and industrial taxpayers generally.
>
> . . .
>
> This particular tax, however, is not on property. It is on the burning of propulsion fuel in part of the transportation industry, the railroads. For relevant comparisons we must thus look to taxpayers who employ propulsion fuel in transportation. This narrows the field of comparison, in the main, to three other transportation modes: trucks, barges and aircraft.

AFC Industries, 961 F.2d at 821.

> Drawing on the analogy of property taxes, the present excise tax must be nondiscriminatory compared with fuel taxes on any of these other modes so as to avoid a competitive disadvantage.

Atchison, Topeka and Santa Fe Railway Co. v. Bair, 338 N.W.2d at 346.

> Comparing state fuel taxation of railroads and of trucks, the railroad tax in question discriminates against the railroads contrary to Section 11503.

Id. at 347.

Similarly, the Supreme Court of Minnesota defined a comparison class to include motor carriers in striking down state sales and use taxes on railroad rolling stock and repair parts.

> The second issue is simply this: if the transaction-based sales and use tax on purchases does apply to railroad rolling stock and repair parts, does that tax discriminate against railroads in violation of federal law?
>
> . . .
>
> To be discriminatory, a tax must be discriminatory as compared to someone else. The commissioner argues that the proper comparison class should be other commercial and industrial taxpayers in general. Burlington Northern, on the other hand, argues that the comparison should be with its transportation competitors. . .. It seems to us that National Railroad Passenger Corp. v. State Board of Equalization, 652 F.Supp. 923 (N.D. Cal. 1986) (the Amtrak case) represents the proper approach . . . The Federal District Court held that the tax violated Section 306 because it applied to passenger rail cars and not to other passenger vehicles used by common carriers in interstate commerce. In other words, the court

> used the railroad's competitors as the comparison class. We think we should do so here too. This approach is in keeping with the purpose of the 4-R Act: to revitalize the railroad industry by making it competitive.

Burlington Northern Railroad v. Commissioner of Revenue, 509 N.W.2d at 553.

> We hold that the exemptions for barges and airplanes, as well as the alternative tax scheme for motor vehicles, make application of Minnesota's general sales and use tax to railroad rolling stock and repair parts discriminatory and illegal under Section 306 of the 4-R Act.

Id. at 554.

These holdings cannot be reconciled with the opinion of the Ninth Circuit in this case.

II. THIS COURT SHOULD HOLD THAT THE ARIZONA TAXES ARE DISCRIMINATORY.

A. The Ninth Circuit Opinion Misinterpreted Supreme Court Precedent.

The Ninth Circuit concluded, erroneously, that the exemption for motor carriers is not discriminatory based on this Court's opinion in ACF Industries. The Ninth Circuit concluded:

> According to ACF, discrimination under the 4-R Act does not arise when exemptions are granted from a generally applicable tax if railroads are treated fairly in comparison to other commercial and industrial taxpayers subject to the tax. The Arizona transaction privilege tax and use tax exemptions for motor carriers do not violate the 4-R Act because the taxes at issue are generally

> applicable and because the railroads are treated fairly in comparison to other taxpayers subject to the Arizona taxes.

78 F.3d at 443-44. This represents a clear misreading and misinterpretation of ACF Industries.

While this Court held that the exemptions at issue in ACF Industries did not violate the 4-R Act, this Court's holding was expressly limited to exemptions from "generally applicable ad valorem property taxes." This Court used such precise language in limiting its opinion at least three separate times. 510 U.S. at ___, 114 S. Ct. at 846, 848, 852. This limitation was appropriate under the facts presented in ACF Industries. In that case, ACF Industries challenged certain property tax exemptions under Section 306(1). The property tax exemptions at issue did not violate the specific property tax limitations applicable under subsections (a)-(c).

In ACF Industries, this Court, however, did compare the broad language of subsection (d) with the specific and detailed property tax provisions in subsections (a)-(c) and the definition of "commercial and industrial property" specifically applicable to subsections (a)-(c). This Court held that Congress did not intend to prohibit, by the general provisions in 306(1)(d), property tax exemptions permitted by the specific provisions on property taxes in subsections (a)-(c). The Court's analysis does not apply to the nonproperty taxes now at issue.

The transaction privilege and use taxes at issue in this case are not the subject of comprehensive regulation elsewhere in the 4-R Act. While Congress treated the ad valorem property taxes with a high degree of precision under the 4-R Act, the same precision was not applied to other forms of tax which may result in discrimination. By its nature, the broad prohibition of Section 306(1)(d) could not focus explicitly and precisely on every possible form of tax discrimination. This Court's opinion in ACF Industries is limited to ad valorem property tax exemptions and offers no bar to the determination reached by the District Court that the transaction privilege and use tax exemptions at issue in this case result in discrimination to the railroads. The Ninth Circuit's decision in this case rests, therefore, on a wholly indefensible misunderstanding of ACF Industries.

B. The Ninth Circuit Opinion Conflicts With Congressional Intent Behind the 4-R Act.

The Ninth Circuit rejected a comparison class of motor carriers and held that:

> The Arizona transaction privilege tax and use tax are taxes of general applicability, and therefore, the exemptions for motor carriers are permissible under the 4-R Act.

78 F.3d at 443. The majority opinion, which failed to recognize the competitive disadvantage resulting from the Arizona tax scheme, cannot be reconciled with the congressional purposes underlying the 4-R Act. The impetus behind the 4-R Act "was to the put the railroads back on an even footing with other forms of transportation." Kansas City Southern Railway v. McNamara, 817 F.2d 368, 374 n.12 (5th Cir. 1987). Congress sought "to revitalize the railroad industry by making it competitive." Burlington Northern Railroad v. Commissioner of Revenue, 509 N.W.2d 551, 553 (Minn. 1993). Allowing Arizona to impose a tax on railroads and not motor carriers is inconsistent with these Congressional objectives.

Arizona imposes a transaction privilege tax on the business of transporting for hire persons, freight or property. Motor carriers are exempt from this tax. Arizona imposes a use tax on out-of-state purchases of diesel fuel to power locomotives. Gasoline and diesel fuel purchased out of state by motor carriers for transportation on Arizona roads are exempt from this use tax. Railroads are subject to taxes to which their competitors are not. This is as clear a violation of the 4-R Act as can be imagined. No previous decision of any court has refused to prevent such discriminatory tax treatment under the 4-R Act.

C. The Arizona State Tax Scheme Cannot be Justified.

In its opinion below, the Ninth Circuit asserted:

> Furthermore, the transaction privilege tax and use tax exemptions for motor carriers do not entirely exempt motor carriers from taxation because motor carriers are taxed under a separate tax scheme.

78 F.3d at 443.

Taxation of motor carriers under a separate tax scheme cannot justify the transaction privilege and use tax exemptions at issue here. A discriminatory tax cannot be justified on the basis that other taxes compensate for the discriminatory effect. Burlington Northern Railroad v. City of Superior, 932 F.2d 1185, 1188 (7th Cir. 1991); Trailer Train Co. v. State Tax Commission, 929 F.2d 1300, 1302 (8th Cir.), cert. denied, 502 U.S. 856 (1991); Kansas City Southern Railway v. McNamara, 817 F.2d 368, 377-78 (5th Cir. 1987).

III. CONCLUSION

Arizona's imposition of a transaction privilege tax and use tax on rail carriers but not motor carriers discriminates against railroads in a manner now unlawful in Iowa and Minnesota. The decision of the United States Court of Appeals for the Ninth Circuit upholds discriminatory tax treatment of the railroads which has never before been held lawful under the 4-R Act. This Court should grant the petition and issue a writ of certiorari to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit.

Dated this 10 day of October, 1996.

CHRISTENSEN & JENSEN, P.C.

Dale J. Lambert,
Counsel of Record for
Petitioner

APPENDIX

Opinion of United States Court of Appeals for the Ninth Circuit, March 4, 1996 ..... App. 1

Judgment of United States District Court for the District of Arizona, March 31, 1994 ..... App. 19

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49 U.S.C. § 11503 ..... App. 25

42 Arizona Revised Statutes §§ 1310.02, 1408, 1409(a)(5) ..... App. 27

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, a Delaware corporation; SOUTHERN PACIFIC TRANSPORTATION COMPANY; ARIZONA CENTRAL RAILROAD,

Plaintiffs-Appellees,

v.

STATE OF ARIZONA; ARIZONA DEPARTMENT OF REVENUE; CITY OF PHOENIX AND TOWN OF CLIFTON,

Defendants-Appellants.

No. 94-15850
D.C. No.
CV-93-00549-RGS

OPINION

Appeal from the United States District Court
for the District of Arizona
Roger G. Strand, District Judge, Presiding

Argued and Submitted
October 19, 1995 - San Francisco, California

Filed March 4, 1996

Before: Warren J. Ferguson and Michael Daly Hawkins,
Circuit Judges, and Wm. Fremming Nielsen,*
District Judge

Opinion by Judge Ferguson
Dissent by District Judge Nielsen

*Honorable Wm. Femming Nielsen, District Judge
for the Eastern District of Washington, sitting by designation.

SUMMARY

Tax/Railroads/State

The court of appeals reversed a district court judgment and remanded. The court held that Arizona's transaction privilege tax and use tax do not violate the Railroad Revitalization and Regulatory Reform Act (4-R Act) merely because they provide an exemption for motor carriers.

Appellant the State of Arizona imposes a transaction privilege tax and a use tax. The transaction privilege tax is similar to a sales tax and is applicable to most businesses in Arizona. The transaction privilege tax is applicable to 17 classifications of industrial and commercial taxpayers. Motor carriers are exempt from the transporting classification of the transaction privilege tax; instead, they are taxed under a separate tax scheme.

Arizona taxing authorities determined that additional transaction privilege taxes were due on appellee Southern Pacific Transportation Co.'s activities within Arizona. Southern Pacific and appellee the Atchison, Topeka and Santa Fe Railway Co. (collectively, the railroads) sued the State of Arizona in district court, seeking a declaratory judgment that the State's transaction privilege tax and use tax were discriminatory in violation of the 4-R Act. The railroads also sought a permanent injunction against further imposition of the taxes. The court granted the railroads' motion for summary judgment, holding that the Arizona tax scheme discriminated against the railroads because the railroads' major competitors, motor carriers, were exempt from the Arizona transaction privilege tax and use tax. The State appealed.

[1] Section 11503(b)(4) of the 4-R Act provides that a state may not impose "another tax" that discriminates against certain rail carriers. [2] Subsection (b)(4) was designed to encompass all discriminatory state taxes, not just discriminatory property taxes or "in lieu" taxes. Therefore, the subsection was applicable to the analysis of Arizona's transaction privilege tax and use tax.

[3] The district court erred in its choice of a comparison class. The proper comparison class to use in analyzing discriminatory taxation of the railroads under the 4-R Act was "all other commercial and industrial taxpayers subject to the taxes." [4] A narrow comparison class, comprised only of "motor carriers," would result in preferential treatment of the railroads.

[5] The Supreme Court previously held that discrimination under the 4-R Act does not arise when exemptions are granted from a generality applicable property tax if railroads are treated fairly in comparison to other industrial and commercial taxpayers subject to the tax. [6] The logic advanced by the Court was equally applicable to the context of transaction privilege tax and use tax exemptions. [7] In this case, the transaction privilege tax and use tax were generally applicable taxes. [8] Following the logic advanced by the Court in its case, the Arizona transaction privilege tax and use tax did not violate the 4-R Act merely because they provided an exemption for motor carriers. [9] In addition, the tax rate imposed on the railroads was equivalent to that imposed on the vast majority of other commercial and industrial taxpayers. [10] The railroads were not singled out for discriminatory taxation through either use of discriminatory tax exemptions or through excessive tax rates.

District Judge Nielsen dissented, stating that the majority utilized an inappfopriate comparison class in determining whether the tax exemption resulted in discrimination against the railroads. District Judge Nielsen stated that the disparate tax treatment of the railroads with motor carriers was discriminatory.

COUNSEL

Paul J. Mooney, Fennemore Craig, Phoenix, Arizona, for the plaintiffs-appellees.

James M. Susa, Deputy Attorney General Phoenix, Arizona, for the defendants-appellants.

OPINION

FERGUSON, Circuit Judge:

The State of Arizona appeals the district court's grant of summary judgment in favor of the plaintiffs. The district court held that Arizona's taxation scheme discriminated against the railroads and therefore violated the Railroad Revitalization and Regulatory Reform Act. We reverse.

I. *Statement of the Case*

A. *Factual Background*

The State of Arizona imposes both a transaction privilege tax and a use tax. Ariz.Rev.Stat.Ann. §§ 42-1301 et seq., 42-1401 et seq. (1991).[1] The Arizona transaction privilege tax, which is similar to a sales tax, is applicable to most businesses in Arizona. It is generally imposed at a rate of five percent on the sale of goods and services occurring in the state. The Arizona use tax is a reciprocal tax which imposes a five percent levy on the price of goods purchased outside the state which are later brought into the State for use, storage, or consumption.

The Arizona transaction privilege tax is applicable to seventeen classifications of industrial and commercial taxpayers.[2] The transporting classification of the transaction privilege tax is defined as "the business of transporting for hire persons, freight

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[1] In addition, most Arizona cities and towns have adopted the Model City Tax Code which imposes a transaction privilege tax similar to the Arizona state transaction privilege tax.

[2] The seventeen classifications of businesses to which the transaction privilege tax applies are: retail sales, transporting, utilities, telecommunications, publication, job printing, pipelines, private car lines, commercial leases, transient lodging, personal property rentals, mining, amusement, restaurant, prime contracting, owner-builder sales and membership camping. Ariz.Rev.Stat.Ann. §§ 42-1310.01-.18 (1991 & Supp.1995).

or property by motor vehicle, railroads or aircraft from one point to another point in this state." Ariz.Rev.Stat.Ann. § 42-1310.02 (1991).

Motor carriers are exempt from the trans-porting classification of the transaction privilege tax because they are taxed under a separate tax scheme. Motor carriers are taxed under Ariz.Rev.Stat.Ann. § 28-1599 et seq. (1989). The motor carrier tax is a weight-distance tax. It is generally calculated by multiplying the number of miles traveled by a motor vehicle on the public highways within the State of Arizona, by the applicable motor carrier tax rate for that motor vehicle's weight class. Ariz.Rev.Stat.Ann. § 28-1599.05(B) (1989). The motor carrier tax is not applicable to the railroads.

B. *Procedural Background*

The State of Arizona Taxing Authorities determined that additional transaction privilege taxes were due on Southern Pacific Transportation Company's activities within Arizona. After two unsuccessful administrative appeals, Southern Pacific and the Atchison, Topeka, and Santa Fe Railroad brought suit in district court. The railroads sought a declaratory judgment that the State of Arizona's transaction privilege tax and use tax were discriminatory in violation of The Railroad Revitalization and Regulatory Reform Act (the "4-R Act"), 49 U.S.C. § 11503 (1988), and a permanent injunction against the further imposition of these taxes for current or subsequent tax periods.[3]

After filing their complaint, Southern Pacific and Santa Fe moved for a preliminary injunction to prohibit the collection of the alleged discriminatory taxes. The district court denied this motion on the basis that discriminatory taxation occurs when the railroads are subject to a tax which applies only to a narrow class of taxpayers. The district court held that because the Arizona transaction privilege tax and use tax were applicable to a broad class of taxpayers, they were not discriminatory.

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[3] The Railroads also challenged the City of Phoenix's and Town of Clifton's transaction privilege taxes in this litigation.

The Taxing Authorities then moved for summary judgment against the railroads. In response, the railroads filed a cross-motion for summary judgment against the Taxing Authorities. The district court granted the railroads' motion for summary judgment, holding that the Arizona tax scheme discriminated against the railroads because the railroads' major competitors, motor carriers, were exempt from the Arizona transaction privilege tax and use tax.

II. *Discussion*

We review a grant of summary judgment de novo. *Jesinger v. Nevada Fed. Credit Union*, 24 F.3d 1127, 1130 (9th Cir.1994). We must determine, viewing the evidence in the light most favorable to the nonmoving party, whether there are any genuine issues of material fact and whether the district court correctly applied the relevant substantive law. *Id.*

Three interrelated issues are raised by this litigation: (1) Is the 4-R Act, which seeks to prevent discriminatory taxation of the railroads, applicable to the Arizona tax scheme? (2) If so, what is the proper comparison class to employ in determining whether the Arizona tax scheme discriminates against the railroads? (3) Does the Arizona tax scheme discriminate against the railroads?

A. *Analysis Under the 4-R Act*

The 4-R Act was enacted by Congress in 1976 to restore financial stability to the railroad system in the United States. *Department of Revenue v. ACF Indus., Inc.*, ___ U.S. ___, ___, 114 S.Ct. 843, 846, 127 L.Ed.2d 165 (1994). Congress' purpose was to revitalize the railroads and protect them from discriminatory taxation. *Id.* The applicability of subsection (b)(4) of the 4-R Act is at issue in the present case.

The provisions of the 4-R Act relevant to this case are as follows:

> (b) The following acts unreasonably burden and discriminate against interstate commerce, and a State,

subdivision of a State, or authority acting for a State or subdivision of a state may not do any of them:

> (1) assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
> (2) levy or collect a tax on an assessment that may not be made under clause (1) of this subsection.
> (3) levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
> (4) impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Commission under subchapter I of chapter 105 of this title.

49 U.S.C. § 11503(b)(1)-(4).

The State of Arizona argues that Section 11503(b)(4) of the 4-R Act is not applicable to the transaction privilege taxes and use taxes at issue in this litigation. Arizona asserts that Section 11503(b)(4) prohibits only "in lieu" taxes imposed on the railroads in place of discriminatory property taxes. Such discriminatory property taxes are prohibited by subsections (b)(1) through (b)(3) of Section 11503.

The State's narrow interpretation of subsection (b)(4) of the 4-R Act has been rejected by many Circuits. In *Richmond, F. & P. R.R. v. Department of Taxation*, 762 F.2d 375, 379-80 (4th Cir.1985), it was held that subsection (b)(4) was unambiguously intended to prohibit all discriminatory taxes imposed on rail carriers. The Fifth Circuit, Eighth Circuit, and Eleventh Circuit have reached similar conclusions regarding the scope of subsection (b)(4). *Kansas City S. Ry. v. McNamara*, 817 F.2d 368, 371-74

(5th Cir.1987) (holding that subsection (b)(4) applied to a state transportation and communications utilities tax imposed on gross receipts of intrastate business and rejecting the state's argument that subsection (b)(4) only applied to in lieu taxes); *Trailer Train Co. v. State Tax Comm'n*, 929 F.2d 1300, 1302 (8th Cir.) (holding that subsection (b)(4) forbids all taxes that discriminate against railroads, and not just discriminatory property taxes), *cert. denied*, 502 U.S. 856, 112 S.Ct. 169, 116 L.Ed.2d 133 (1991); *Trailer Train Co. v. State Bd. of Equalization*, 710 F.2d 468, 472 n. 6 (8th Cir. 1983); *Ogilvie v. State Bd. of Equalization*, 657 F.2d 204, 210 (8th Cir.), *cert. denied*, 454 U.S. 1086, 102 S.Ct. 644, 70 L.Ed.2d 621 (1981); *Alabama Great S. R.R. v. Eagerton*, 663 F.2d 1036, 1040 (11th Cir. 1981).

[1] We hold that subsection (b)(4) of the 4-R Act is designed to encompass all discriminatory state taxes, not just discriminatory property taxes or in lieu taxes. Therefore, subsection (b)(4) is applicable to the analysis of Arizona's transaction privilege tax and use tax at issue in this case.

B. *The Choice of Comparison Class*

[2] In determining whether the Arizona taxes discriminate against the railroads, the district court compared the treatment of the railroads with the treatment of their major competitors, motor carriers. The district court erred in its choice of a comparison class. We hold that the proper comparison class to use in analyzing discriminatory taxation of the railroads under the 4-R Act is "all other commercial and industrial taxpayers subject to the taxes."

Many courts have already employed the comparison class of "other commercial and industrial taxpayers subject to the tax" in analyzing subsection (b)(4) of the 4-R Act. In *Kansas City S. Ry. v. McNamara*, 817 F.2d 368 (5th Cir.1987), the court stated:

> The only simple way to prevent tax discrimination against the railroads is to tie their tax fate to the fate of a large and local group of taxpayers. . . . We think the best course is to require that the railroads be taxed only under

> taxes applicable to *'other commercial and industrial' taxpayers.*

Id. at 375 (emphasis added). Similarly, the Seventh Circuit held that "a tax is 'discriminatory' within the meaning of the fourth subsection of the 4-R Act if it imposes a proportionately heavier tax on railroading *than on other activities*." *Burlington N.R.R. v. City of Superior*, 932 F.2d 1185, 1187 (7th Cir.1991) (emphasis added). Following the logic of the Fifth and Seventh Circuits, the proper comparison class for determining whether the Arizona transaction privilege tax and use tax violate subsection (b)(4) of the 4-R Act is "all industrial and commercial taxpayers who are subject to the tax."

[3] Moreover, the purpose of the 4-R Act was not to grant railroads preferential treatment. *CSX Transp., Inc. v. Tennessee State Bd. of Equalization*, 801 F.Supp. 28, 35-36 (M.D.Tenn.1992). Rather, in adopting the 4-R Act, Congress' purpose was to remedy discrimination against the railroads and place them on an even playing field with other state taxpayers. *Ogilvie v. State Bd. of Equalization*, 657 F.2d 204, 207 (8th Cir.), *cert. denied*, 454 U.S. 1086, 102 S.Ct. 644, 70 L.Ed.2d 621 (1981). This goal was reflected in the Association of American Railroads' proposed antidiscrimination tax bill which later served as the basis for the 4-R Act:

> This proposed antidiscrimination tax bill, . . . has the obvious merit of insuring that such carriers would receive equal treatment *with other taxpayers subject to the same tax rates* in accordance with applicable State law. The proposal in no way alters the freedom of the State to tax its taxpayers as in its discretion it deems best, so long as such carriers are *accorded equal tax treatment with other taxpayers.*

Ogilvie, 657 F.2d at 207 n. 3 (emphasis added) (quoting S.Rep. No. 445, 87th Cong., 1st Sess. 465-66 (1961)). *But cf. Burlington Northern R.R. Co. v. Triplett*, 682 F. Supp. 443, 446 (D.Minn.1988); *National R.R. Passenger Corp. v. State Bd. of Equalization of Cal.*, 652 F.Supp. 923, 926-27 (N.D.Cal.1986);

Burlington Northern R.R. Co. v. Commissioner of Revenue, 509 N.W.2d 551, 553-54 (Minn.1993); *Atchison, Topeka & Santa Fe Ry. v. Bair*, 338 N.W.2d 338, 346 (Iowa 1983).

The comparison class of "commercial and industrial taxpayers subject to the tax" must be used in analyzing the Arizona tax scheme because a narrow comparison class, comprised only of "motor carriers," would result in preferential treatment for the railroads. In order for railroad carriers to receive equal treatment with other taxpayers subject to the same tax law, they must be compared to all others subject to the tax in question, not just compared to motor carriers. Although subsection (b)(4) is silent as to the proper comparison class, congressional intent behind the 4-R Act dictates that the comparison class of "other commercial and industrial taxpayers subject to the tax" be used. *See Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 51, 107 S.Ct. 1549, 1555, 95 L.Ed.2d 39 (1987) (holding that in interpreting status, courts must not be guided by a single sentence, but must look to the provisions of the whole law and to its object and policy).

C. *Discriminatory Taxation Analysis*

In claiming that the Arizona transaction privilege tax and use tax are discriminatory, the railroads make two arguments: 1) the Arizona transaction privilege tax and use tax exemption for motor carriers is discriminatory; and 2) the Arizona transaction privilege tax and use tax impose discriminatory rates upon the railroads. Both of these arguments lack merit.

[4] First, the discriminatory exemption argument fails because the Supreme Court, in *Department of Revenue v. ACF Indus., Inc.*, — U.S. —, —, 114 S.Ct. 843, 846, 127 L.Ed.2d 165 (1994), held that discrimination under the 4-R Act does not arise when exemptions are granted from a generally applicable property tax if the railroads are treated fairly in comparison to other industrial and commercial taxpayers subject to the tax. "[A] State may grant exemptions from a generally applicable ad valorem property tax without exposing the taxation of railroad property to invalidation under subjection (b)(4)." *Id.* at —, 114 S.Ct. at 848. "It would be illogical to conclude that Congress,

having allowed the States to grant property tax exemptions in subsections (b)(1)-(3), would turn around and nullify its own choice in subsection (b)(4). . . . *Id.* at ---, 114 S.Ct. at 849. *See also, Burlington N. R.R. v. Wisconsin Dept. of Revenue*, 59 F.3d 55, 58 (7th Cir.1995) (holding that exempting eighty percent of non-railroad commercial and industrial property from a generally applicable ad valorem property tax did not violate the 4-R Act); *cf. Burlington N. R.R. v. Bair*, 60 F.3d 410, 413 (8th Cir.1995) (The court held that Iowa's real property tax violated subsection (b)(4) of the 4-R Act and did not fall within the exemption exception carved out in *ACF* because the tax was not one of general applicability. The court determined that Iowa's real property tax was discriminatory because it singled out for taxation all personal property of the railroads, while leaving untaxed most of the personal property of the majority of commercial and industrial enterprises in the state).

Although *ACF* specifically addressed property tax exemptions, the logic advanced by the Supreme Court is equally applicable to the context of transaction privilege tax and use tax exemptions. The Court in *ACF* reasoned that if Congress, as a condition of permitting the taxation of railroad property had intended to restrict state power to exempt non-railroad property, Congress would have done so with clarity and precision. *ACF*, --- U.S. at ---, 114 S.Ct. at 850. The Court further explained that in determining the breadth of a federal statute which impinges upon a State's traditional powers, courts should be hesitant to extend a statute beyond its evident scope. *Id.* Accordingly, if Congress, as a condition of permitting state taxation of the railroads through sales and use taxes had intended to restrict state power to exempt other types of businesses from these taxes, Congress would have done so explicitly. Therefore, because Congress did not explicitly prohibit states from carving out exemptions to their sales and use taxes, such exemptions are permissible.

[5] The transaction privilege tax and use tax at issue in this case are generally applicable taxes. The transaction privilege tax is imposed upon seventeen classifications of business activities, including railroad activities, and encompasses over 140,000 industrial and commercial taxpayers. The Arizona use tax is imposed on all businesses in Arizona, irrespective of

whether the business is additionally subject to the transaction privilege tax. The number of businesses subject to the use tax is so large that the Taxing Authorities cannot provide an exact number. However, they are confident that the number exceeds the 140,000 taxpayers subject to the transaction privilege tax.

Following the logic advanced by the Supreme Court in *ACF*, the Arizona transaction privilege tax and use tax do not violate the 4-R Act merely because they provide an exemption for motor carriers. The Arizona taxation privilege tax and use tax are taxes of general applicability, and therefore, the exemptions for motor carriers are permissible under the 4-R Act. Furthermore, the transaction privilege tax and use tax exemptions for motor carriers do not entirely exempt motor carriers from taxation because motor carriers are taxed under a separate tax scheme.

[6] The second argument advanced by the railroads is that the Arizona tax scheme is discriminatory because the railroads are subjected to discriminatory tax rates. This argument fails as well. The tax rate imposed on the railroads is equivalent to that imposed on the vast majority of other commercial and industrial taxpayers. The transaction privilege tax rate of five percent applies to fourteen of the seventeen classifications of businesses subject to the tax. Those fourteen classifications comprise approximately seventy-nine percent of the total transaction privilege tax collected by the State of Arizona.

[7] Lastly, the railroads argue that the Arizona tax scheme is discriminatory because the revenue collected from motor carrier taxes is used to repair the roads, while the railroads must repair trackage themselves. This argument is without merit. The Arizona Constitution allows taxes to be "levied and collected for public purposes only." Ariz. Const. art. 9, § 1 (1984) (Ariz. Rev.Stat.Ann.). *See City of Phoenix v. Michael*, 61 Ariz. 238, 239, 148 P.2d 353, 354 (1944) (holding that a city may not expend public money except for public purposes, and then only when directly or impliedly authorized to do so). The State of Arizona cannot levy and collect taxes to construct and maintain trackage on privately owned railroad property. The 4-R Act reaches only tax burdens and not tax benefits.

In sum, the railroads have not been singled out for discriminatory taxation through either the use of discriminatory tax exemptions or through excessive tax rates. According to *ACF*, discrimination under the 4-R Act does not arise when exemptions are granted from a generally applicable tax if the railroads are treated fairly in comparison to other commercial and industrial taxpayers subject to the tax. The Arizona transaction privilege tax and use tax exemptions for motor carriers do not violate the 4-R Act because the taxes at issue are generally applicable and because the railroads are treated fairly in comparison to other taxpayers subject to the Arizona taxes. The tax rates imposed by Arizona are also not discriminatory. The railroads pay the same tax rate as fourteen of the seventeen classifications subject to the transaction privilege tax.

III. *Conclusion*

The district court's grant of summary judgment for the plaintiffs is REVERSED. The district court's grant of a permanent injunction for the plaintiffs is REVERSED. We REMAND and direct the district court to grant summary judgment in favor of the defendants.

WM. FREMMING NIELSEN, District Judge, dissenting:

I concur with the Court's holding in respect to Section II A. However, I respectfully dissent because the majority utilizes an inappropriate comparison class in determining whether this tax exemption results in discrimination against the Railroads. I would AFFIRM the district court's holding that the correct comparison group is the Railroad's competitors, and that the tax discriminates against the Railroads.

I believe that using the competitor comparison class in this case serves the purpose of (1) harmonizing what appears to be a conflict amongst the courts regarding the appropriate comparison class under 306(1)(d); (2) making statutory sense of 306(1) which provides a specific comparison class in three of four subsections, but pointedly omits any reference to a comparison class in the subsection at issue here; (3) upholding the purposes of the 4-R Act

in avoiding adverse competitive effects against the railroads; and (4) avoiding the patently discriminatory effects of this tax.

I.

The majority cites two cases supporting the broad comparison group. *Burlington Northern R.R. Co. v. City of Superior*, 932 F.2d 1185, 1187 (7th Cir.1991); *Kansas City So. Ry. v. McNamara*, 817 F.2d 368, 376 (5th Cir.1987), but does not address the three courts that adopt the competitor comparison class. *Burlington Northern R.R. Co. v. Triplett*, 682 F.Supp. 443, 446 (D.Minn.1988); *Burlington Northern R.R. Co. v. Commissioner of Revenue*, 509 N.W.2d 551, 553-54 (Minn.1993); *Atchison, Topeka & Santa Fe Ry v. Bair*, 338 N.W.2d 338, 346 (Iowa 1983). The majority makes no attempt to reconcile these cases. I believe that a harmonization of these seemingly opposite cases is not only possible, but necessary to make sense of the statute. An examination of the cases considering this issue suggests that tax discrimination under 306(1)(d) of the 4-R Act has been rejected in two district situations, which necessarily dictate different comparison classes.

Two Circuits embraced the "other commercial and industrial taxpayer" comparative class under 306(1)(d) when railroads were essentially singled out for taxation. *Burlington Northern R.R. Co. v. City of Superior*, 932 F.2d at 1187, or the class of taxpayers burdened by the tax was "unnecessarily small." *McNamara*, 817 F.2d at 376. In these situations, the appropriate comparison class is composed of general commercial and industrial taxpayers subject to the tax because the essence of the railroads' claim is that the railroads are singled out of that class for differential treatment.

This case, however, involves a broad tax that exempts the Railroads' primary competitors. The majority's reliance on *McNamara* and *Burlington Northern v. City of Superior* is misplaced because neither case addresses this form of discriminatory taxation. *Burlington Northern R.R. Co. v. Commissioner of Revenue*, 509 N.W.2d at 553. The use of the "other commercial and industrial taxpayer" class in this setting is ineffectual because it allows precisely the type of discriminatory

tax at issue here. Indeed, the majority does not cite to a single case upholding a general tax that includes a railroad, but excludes the railroad's primary competitors. Such a case does not exist because the discriminatory results are obvious. In this type of situation, then, the appropriate comparison class must be the railroad's competitors.

II.

Two comparison groups may be utilized under subsection (d) because that subsection does not require that a specific comparison group be adopted. This is in marked contrast to subsections (a), (b), and (c) which require that commercial and industrial taxpayers be used as the comparison class. Indeed, the Ninth Circuit previously noted this omission in subsection (d):

> [S]ections 3061(a) and (c), . . . restrict the comparison classes to "other commercial and industrial property." There is no analogous restriction in the broad language of section 3061(d).

ACF Indus. Inc. v. Department of Revenue, 961 F.2d 813, 821 (9th Cir.1992) *rev'd on other grounds*, --- U.S. ----, 114 S.Ct. 843, 127 L.Ed. 2d 165 (1994).

The majority glosses over this statutory construction problem by arguing that Congressional intent "dictates" the broad comparison class be used under subsection (d). Putting aside the question of Congressional intent for a moment, this does not explain why Congress specifically chose to omit any reference to a comparison class in subsection (d), yet utilized the "other commercial and industrial" taxpayer group in subsections (a), (b), and (c). I believe a more careful analysis of the statutory construction issue is necessary in order to help discern Congressional intent.

The Supreme Court has addressed the issue of statutory omissions. *Federal Trade Comm'n v. Sun Oil Co.*, 371 U.S. 505, 513-515, 83 S.Ct. 358, 363-364, 9 L.Ed.2d 466 (1963). In *Sun Oil Company*, the Court considered two subsections of a statute, the second part of which omitted a detailed description of "competition" that existed in subsection (a). *Id.* The Court

refused to construe subsection (b) as having the same definition, holding that "(t)here is no reason appearing on the face of the statute to assume that Congress intended to invoke by omission in 2(b) the same broad meaning of competition or competitor which it explicitly provided by inclusion in 2(a); **the reasonable inference is quite the contrary.**" *Id.* at 515, 83 S.Ct. at 365 (emphasis added).

Therefore, I proceed with the assumption that the omission of a comparison class in 306(1)(d) is not coincidental. If Congress wanted that subsection to share the same broad comparison class as the three preceding sections, and none other, it would have said so. It did not. *Sun Oil Co.*, 371 U.S. at 514-515, 83 S.Ct. at 364 ("[S]ince Congress expressly demonstrated in the immediately preceding provision of the Act that it knew how to expand the applicable concept of competition . . . it is reasonable to conclude that like clarity of expression would be present in 2(b). . . .") I refuse to provide for an exclusive comparison class under 306(1)(d) when congress explicitly chose not to do so. Finding that 306(1)(d) only permits the broad comparison class does not interpret the 4-R Act, but amends it. *Fedorenko v. United States*, 449 U.S. 490, 513, 101 S.Ct. 737, 750, 66 L.Ed.2d 686 (1981) (citing *Sun Oil Co.*, 371 U.S. at 514-515, 83 S.Ct. at 364-365).

III.

"The purpose of the 4-R Act was to prevent tax discrimination against railroads in any form whatsoever." *Ogilvie v. State Board of Equalization*, 657 F.2d 204, 210 (8th Cir.), *cert. denied*, 454 U.S. 1086, 102 S.Ct. 644, 70 L.Ed.2d 621 (1981) (emphasis added). The rationale for the Act is the concern that railroads "'are easy prey for states and local tax assessors in that they are non-voting, often non-resident, targets for local taxation, who cannot easily remove themselves from the locality.'" *Id.* (citations omitted).

The Broad comparison group defeats the purpose of the 4-R Act by placing the Railroads at a decided competitive disadvantage. *Burlington Northern R.R. v. Commissioner of Revenue*, 509 N.W.2d at 553 (comparison class "is in keeping

with the purpose of the 4-R Act: to revitalize the railroad industry by making it competitive"); *Triplett*, 682 F.Supp. at 446. Where the majority sees "preferential treatment" for the Railroads, I see a tax that hinders the Railroads' ability to compete fairly with its competitors. I do not object to the Railroads paying their fair share of the tax burden. I do object, however, to the payment of discriminatory taxes which place the Railroads at a decided competitive disadvantage.

IV.

The weakness of the exclusive use of the broad comparison class becomes evident in a case like this. The transaction privilege tax reaches over 140,000 transaction privilege tax licenses issued statewide. There is one exception. That exception, of course, is for motor carriers who represent the principal competitors of the Railroads. As the Fourth Circuit noted, "in essence, discrimination is a failure to treat all persons equally where no reasonable distinction can be found between those favored and those not favored." *Richmond, Fredericksburg & Potomac R.R. v. Department of Taxation*, 762 F.2d 375, 380 n. 4 (4th Cir.1985). I fail to find such a distinction in the case before us.

The broad comparison class overlooks the obvious point that a tax imposed on rail carriers, but not on motor carriers, is discriminatory in the most basic sense of the word -- it treats those engaged in an identical activity differently. In this instance, it treats those involved in the transportation of goods or passengers differently, and the Railroads suffer a dramatic competitive disadvantage. This is a result the 4-R Act cannot allow.

The disparate tax treatment of the Railroads with motor carriers, their principal competitor, is discriminatory. This disparate treatment is, in my view, unlawful under the 4-R Act. Accordingly, I DISSENT.

UNITED STATES DISTRICT COURT

DISTRICT OF ARIZONA

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, a Delaware corporation; et al.	NO.CIV 93-0549 PHX RGS NO.CIV 93-0553 PHX RGS NO.CIV 93-1562 PHX RGS (Consolidated)
Plaintiffs,	
v.	**JUDGMENT**
STATE OF ARIZONA, ET AL.,	
Defendants.	

This action came on for hearing on February 28, 1994 on cross-motions for summary judgment. Plaintiff The Atchison, Topeka, and Santa Fe Railway Company ("Santa Fe") appeared by its attorneys Fennemore Craig by Paul J. Mooney and Ray K. Harris. Plaintiff Southern Pacific Transportation Company ("Southern Pacific") appeared by its attorneys Gallagher & Kennedy by Dean C. Short, II. Defendants appeared by the Arizona Attorney General by Tracy S. Essig and James J. Susa.

The court, having considered the written memoranda submitted by the parties and the oral arguments of counsel, finds that there is no genuine issue of material fact and plaintiffs are entitled to judgment as a matter of law.

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that the permanent injunction attached hereto is entered against defendants the State of Arizona, the City of Phoenix and the Town of Clifton.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED, that plaintiffs' cross-motion for summary judgment is granted and declaratory judgment is hereby entered pursuant to

28 U.S.C. § 2201 in favor of plaintiffs on all three counts of the Complaint as follows:

1. The Arizona transaction privilege tax on the transporting classification (A.R.S. § 42-1310.02) unlawfully discriminates against plaintiffs in violation of 49 U.S.C. § 11503(b)(4);

2. The Arizona use tax (A.R.S. § 42-1408) unlawfully discriminates against plaintiffs in violation of 49 U.S.C. § 11503(b)(4) insofar as it applies to purchases of diesel fuel and materials and equipment to construct and maintain the rail lines.

3. The local transaction privilege tax on transporting for hire (Model City Tax Code § 475) unlawfully discriminates against plaintiffs in violation of 49 U.S.C. § 11503(b)(4).

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that jurisdiction is retained over this action for the purposes of taxing costs, considering any application for attorneys' fees, and enforcing the permanent injunction entered herewith.

DATED: March 30, 1994.

/s/
ROGER G. STRAND
U.S. District Court Judge

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, a Delaware corporation; SOUTHERN PACIFIC TRANSPORTATION COMPANY; ARIZONA CENTRAL RAILROAD,	)	NO. 94-15850
Plaintiffs-Appellees,	)	ORDER
v.	)	
STATE OF ARIZONA, ARIZONA DEPARTMENT OF REVENUE; CITY OF PHOENIX AND TOWN OF CLIFTON,	)	
Defendants-Appellants.	)	

Before: FERGUSON and HAWKINS, Circuit Judges, and NIELSEN,*

The Motion to Join in Petition for Rehearing and Suggestion for Rehearing En Banc filed by Arizona Central Railroad, Inc. is GRANTED.

Judges Ferguson and Hawkins have voted to deny the petition for rehearing and recommend the denial of the en banc request. Judge Nielsen has voted to grant the petition for rehearing suggestion for rehearing en banc.

The full court has been advised of the suggestion for en banc hearing and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35.

The petition for rehearing is DENIED and the suggestion for a rehearing en banc is REJECTED.

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* Honorable Wm. Fremming Nielsen, District Judge for the Eastern District of Washington, sitting by designation.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

NO. 94-15850
CT/AG#: CV-93-00549-RGS

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY a Delaware corporation, et al.; SOUTHERN PACIFIC TRANSPORTATION COMPANY; ARIZONA CENTRAL RAILROAD

Plaintiffs - Appellees

v.

STATE OF ARIZONA; ARIZONA DEPARTMENT OF REVENUE; CITY OF PHOENIX, AND TOWN OF CLIFTON

Defendants - Appellants

APPEAL FROM the United States District Court for the District of Arizona (Phoenix).

THIS CAUSE came on to be heard on the Transcript of the Record from the United States District Court for the District of Arizona (Phoenix) and was duly submitted.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and hereby is REVERSED and REMANDED.

Filed and entered March 4, 1996.

§ 14. Use and distribution of vehicle, user, and gasoline and diesel tax receipts

Section 14. No moneys derived from fees, excises, or license taxes relating to registration, operation, or use of vehicles on the public highways or streets or to fuels or any other energy source used for the propulsion of vehicles on the public highways or streets, shall be expended for other than highway and street purposes including the cost of administering the State highway system and the laws creating such fees, excises, or license taxes, statutory refunds and adjustments provided by law, payment of principal and interest on highway and street bonds and obligations, expenses of State enforcement of traffic laws and State administration of traffic safety programs, payment of costs of publication and distribution of Arizona Highways magazine, State costs of construction, reconstruction, maintenance or repair of public highways, streets or bridges, costs of rights of way acquisitions and expenses related thereto, roadside development, and for distribution to counties, incorporated cities and towns to be used by them solely for highway and street purposes including costs of rights of way acquisitions and expenses related thereto, construction, reconstruction, maintenance, repair, roadside development, of county, city and town roads, streets and bridges and payment of principal and interest on highway and street bonds. As long as the total highway user revenues derived equals or exceeds the total derived in the fiscal year ending June 30, 1970, the State and any county shall not receive from such revenues for the use of each and for distribution to cities and towns, fewer dollars than were received and distributed in such fiscal year. This section shall not apply to moneys derived from the automobile license tax imposed under section 11 of article IX of the Constitution of Arizona. All moneys collected in accordance with this section shall be distributed as provided by law. Addition approved election Nov. 4 1952, eff. Nov. 24, 1952; Amendment approved election No. 3, 1970, eff. Nov. 27, 1970.

§ 11503. Tax discrimination against rail transportation property

(a) In this section--

(1) "assessment" means valuation for a property tax levied by a taxing district.

(2) "assessment jurisdiction" means a geographical area in a State used in determining the assessed value of property for ad valorem taxation.

(3) "rail transportation property" means property, as defined by the Interstate Commerce Commission, owned or used by a rail carrier providing transportation subject to the jurisdiction of the Commission under subchapter I of chapter 105 of this title.

(4) "commercial and industrial property" means property, other than transportation property and land used primarily for agricultural purposes or timber growing, devoted to a commercial or industrial use and subject to a property tax levy.

(b) The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:

(1) assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.

(2) levy or collect a tax on an assessment that may not be made under clause (1) of this subsection.

(3) levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

(4) impose another tax that discriminates against a rail carrier providing transportation subject to the

jurisdiction of the Commission under subchapter I of chapter 105 of this title.

(c) Notwithstanding section 1341 of title 28 and without regard to the amount in controversy or citizenship of the parties, a district court of the United States has jurisdiction, concurrent with other jurisdiction of courts of the United States and the States, to prevent a violation of subsection (b) of this section. Relief may be granted under this subsection only if the ratio of assessed value to true market value of rail transportation property exceeds by at least 5 percent, the ratio of assessed value to true market value of other commercial and industrial property in the same assessment jurisdiction. The burden of proof in determining assessed value and true market value is governed by State law. If the ratio of the assessed value of other commercial and industrial property in the assessment jurisdictional property cannot be determined to the satisfaction of the district court through the random-sampling method known as a sales assessment ratio study (to be carried out under statistical principles applicable to such a study), the court shall find, as a violation of this section-

(1) an assessment of the rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the assessed value of all other property subject to a property tax levy in the assessment jurisdiction has to the true market value of all other commercial and industrial property; and

(2) the collection of an ad valorem property tax on the rail transportation property at a tax rate that exceeds the tax ratio rate applicable to the tax property in the taxing district.

(Pub.L. 95-473, Oct. 17, 1978, 92 Stat. 1445.)

§ 42-1310.02. Transporting classification

A. The transporting classification is comprised of the business of transporting for hire persons, freight or property by motor vehicle, railroads or aircraft from one point to another point in this state. The transporting classification does not include:

1. Transporting for hire persons, freight or property by motor carriers or lightweight motor vehicles subject to a tax under title 28, chapter 9, article 6.[1]

2. The business of transporting for hire persons traveling in air commerce by aircraft if taxation of the business is preempted by federal law.

3. Ambulances or ambulance services provided under title 48 or certified pursuant to title 36, chapter 21.1[2] or provided by a city or town in a county with a population of less than one hundred fifty thousand persons as determined in the most recent United States decennial census.

4. Public transportation program services for the dial-a-ride programs and special needs transportation services.

B. The tax base for the transporting classification is the gross proceeds of sales or gross income derived from the business, except that the gross proceeds of sales or gross income derived from transporting for hire persons, freight or property by a railroad pursuant to a contract with another railroad that is also considered to be engaged in the businesses of transporting persons, freight or property for hire shall be deducted from the tax base if the other railroad is liable for the tax on gross

[1] Section 28-1599 et seq.

[2] Sections 48-101 et seq., and 36-2201 et seq.

proceeds of sales or gross income attributable to the transportation.

Amended by Laws 1994, Ch. 92, § 1; Laws 1994, Ch. 328, § 3.

§ 42-1408. Levy of tax; tax rate; purchaser's liability

A. There is levied and imposed an excise tax on the storage, use or consumption in this state of tangible personal property from a retailer, as a percentage of the sales price.

B. The tax imposed by this section applies to any purchaser which purchased tangible personal property for resale but subsequently uses or consumes the property.

C. The tax rate shall equal the rate of tax applied to retailers according to the respective classification under article 1 of this chapter for the same type of transaction or business activity.

D. Every person storing, using or consuming in this state tangible personal property purchased from a retailer is liable for the tax. The person's liability is not extinguished until the tax has been paid to this state.

E. A receipt from a retailer who maintains a place of business in this state or from a retailer who is authorized by the department to collect the tax, under such rules as it may prescribe, and who is for the purposes of this article regarded as a retailer maintaining a place of business in this state, given to the purchaser as provided in § 42-1411 is sufficient to relieve the purchaser from further liability for the tax to which the receipt refers.

Amended by Laws 1992, Ch. 162, § 5.

§ 42-1409. Exemptions

A. The tax levied by this article does not apply to the storage, use or consumption in this state of the following described tangible personal property:

* * *

5. Motor vehicle fuel and use fuel, the sales, distribution or use of which in this state is subject to the tax imposed under the provisions of title 28, chapter 9, article 1 or 2,[2] use fuel which is sold to or used by a person holding a valid single trip sue fuel tax permit issued under § 28-1559, aviation fuel, the sales, distribution or use of which in this state is subject to the tax imposed under § 28-1765.01 and jet fuel, the sales, distribution or use of which in this state is subject to the tax imposed under chapter 9.2 of this title.[3]

* * *

[2] Sections 28-1501 et seq. or 28-1551 et seq.

[3] Section 42-1571 et seq.

(2)

Supreme Court, U.S.
FILED
NOV 8 1996
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No. 96-586

In The

Supreme Court of the United States

October Term, 1996

ARIZONA CENTRAL RAILROAD,

Petitioner,

v.

STATE OF ARIZONA; ARIZONA DEPARTMENT OF REVENUE; CITY OF PHOENIX; AND TOWN OF CLIFTON,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether Respondents may grant exemptions from generally applicable sales and use taxes imposed uniformly upon railroads and more than 146,000 other commercial and industrial taxpayers, without subjecting such taxation of railroads to challenge under 49 U.S.C. § 11503(b)(4).

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RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondents, the State of Arizona, the Arizona Department of Revenue, the City of Phoenix, and the Town of Clifton (collectively, the "Taxing Authorities"), respectfully request that this Court deny Arizona Central Railroad's Petition for a Writ of Certiorari seeking review of the court of appeals' decision in this case.

STATEMENT OF THE CASE

This tax case concerns an issue of statutory construction that this Court recently resolved and that the circuit courts of appeals have applied consistently.

The sole Petitioner, Arizona Central Railroad, operates a railroad exclusively in Arizona.[1] Its operations focus primarily on providing entertainment rides in Arizona's scenic Verde Valley, although Petitioner also transports some freight along its short route. Petitioner, like more than 146,000 other Arizona businesses, is obligated to pay sales and use taxes. Petitioner objects to paying taxes on its freight income, asserting that Arizona's sales and use tax system discriminates against railroads in violation of the Railroad Revitalization and Regulatory Reform Act of 1976, 49 U.S.C. § 11503 ("4-R Act").

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[1] The other Plaintiffs/Appellees below, Atchison, Topeka and Santa Fe Railway Company ("Santa Fe") and Southern Pacific Transportation Company ("Southern Pacific"), did not file a Petition for Certiorari, and they did not join in the Petition for Certiorari filed by Arizona Central.

The Ninth Circuit Court of Appeals, consistent with decisions by the Seventh, Eighth, and Tenth Circuit Courts of Appeals, correctly applied this Court's decision in *Department of Revenue v. ACF Industries, Inc.*, 510 U.S. 332 (1994), that a State may grant exemptions from a generally applicable tax without subjecting the taxation of railroads to challenge under the relevant provision of the 4-R Act, 49 U.S.C. § 11503(b)(4). The rule in *ACF* establishes that the proper comparison class for determining violations of 49 U.S.C. § 11503(b)(4) is "all other commercial and industrial taxpayers subject to taxes" and not just a railroad's competitors. In applying this rule, the Ninth Circuit determined that Arizona's sales and use tax system does not violate the 4-R Act because railroads pay under the same system of sales and use tax applied to more than 146,000 other Arizona businesses.

The Ninth Circuit applied the *ACF* decision properly. No conflict exists between the circuits. The three pre-*ACF* decisions that Petitioner cites to propose an alternative test are based on false reasoning. In short, no compelling reason exists for this Court to grant the petition.

A. Procedural History.

The procedural history outlined by Petitioner is incomplete. The case began in 1993 when Santa Fe and Southern Pacific – after two unsuccessful state administrative appeals – filed suit seeking a declaration that the Taxing Authorities' sales and use taxes violated federal law and requesting an injunction against the collection of such taxes. Santa Fe and Southern Pacific moved for a preliminary injunction to halt collection of the challenged

taxes during the pendency of the litigation. (Item of Record ("IR") 5.) The court denied the requested preliminary injunction, finding that the railroads had not established "reasonable cause" for the court to believe that a violation of the law was occurring or was about to occur. (IR 37.) The court applied the test in *Kansas City Southern Railway Company v. McNamara*, 817 F.2d 368 (5th Cir. 1987), that discrimination against railroads occurs when a tax is applied to railroads alone or to railroads as part of a narrow class of taxpayers. The court specifically rejected the railroads' argument that a tax is discriminatory if it is applied to the railroads but not to their competitors. (IR 37.) The Taxing Authorities then moved for summary judgment against the railroads. (IR 43.) At this point in the litigation, Petitioner moved to intervene.[2]

In the summary judgment proceedings, the Taxing Authorities furnished the district court with a plethora of statistical information relating to the taxes that they collected in an effort to demonstrate, consistent with *McNamara*, that they impose the taxes at issue upon a broad class of industrial and commercial entities. (IR 43.) The railroads responded by reiterating their assertion concerning discrimination based upon competitive disadvantage. (IR 61.) The district court – without explanation –

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[2] From its intervention in 1993 until the filing of its improper Petition for Certiorari in August 1996 (which the Clerk of this Court returned due to non-compliance with the Court's rules), Petitioner did not initiate anything substantive in this litigation, choosing instead to simply join the pleadings that Santa Fe and Southern Pacific filed.

changed the test that it had used in denying the preliminary injunction and adopted the railroads' competitive disadvantage test that no circuit court had applied. The district court then concluded that the taxes at issue were discriminatory solely because they applied to the railroads and not to their competitors. (IR 85.)

The Taxing Authorities appealed to the Ninth Circuit Court of Appeals, which applied this Court's decision in *ACF* that discrimination would occur only if railroads were taxed as part of an isolated group rather than under taxes that were generally applicable to a large number of taxpayers. The Ninth Circuit determined that the railroads had not been singled out for taxation and that the railroads' placement in a class of more than 146,000 other taxpayers constituted a sufficiently large group to make the sales and use taxes in question generally applicable and thus non-discriminatory. This approach, the court reasoned, would effectuate the congressional purpose of insuring railroads "equal [tax] treatment with other taxpayers." Pet. App. at 10.

B. Factual Background.

Arizona, like most States, relies on three principal taxes to fund government operations. It imposes a property tax, an income tax (both individual and corporate), and a sales tax (technically referred to as the transaction privilege tax). Ariz. Rev. Stat. Ann. ("A.R.S.") §§ 42-201, 43-1001, 43-1101, and 42-1301. Like most States, Arizona also has enacted a use tax that complements the sales tax. *See* A.R.S. § 42-1401.

The State sales tax is imposed at a rate of five percent on the sale of a number of goods and services occurring in Arizona. A.R.S. § 42-1317(A)(1).[3] The use tax also imposes a five percent levy, but on the purchase price of goods bought outside Arizona and later brought into the State for use, storage, or consumption. A.R.S. § 42-1408(A). Although the sales and use taxes are separate taxes, only one can be applied to a transaction. A.R.S. § 42-1409(A)(1).

The sales tax applies to eighteen classes of industrial and commercial entities.[4] To conduct business lawfully in Arizona, an entity must obtain a sales tax license. A.R.S.

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[3] The sales tax is a tax on the privilege of doing business and is "measured by the amount or volume of business transacted by persons on account of their business activities, and in the amounts to be determined by the application of rates against values, gross proceeds of sales or gross income, as the case may be, as prescribed by [statute]." A.R.S. § 42-1306(A). Certain items are exempt from the sales tax, such as prescription medicine (A.R.S. § 42-1310.01(A)(8)) and food (A.R.S. § 42-1310.01(A)(15)).

[4] The eighteen classifications include retail sales, **transporting**, utilities, telecommunications, publication, job printing, pipelines, private car lines, commercial lease, transient lodging, personal property rental, mining, amusement, restaurant, animal feed, prime contracting, owner builder sales, and membership camping. A.R.S. § 42-1310.01-.18. (The court of appeals referred to "seventeen" classifications because it omitted the animal feed classification in its decision. *See* Pet. App. at 5.) The "**transporting**" classification of A.R.S. § 42-1310.02 includes railroads and the operators of ambulances, limousines, buslines, delivery services, moving and van lines, air freight services, shuttles, messenger services, trucking services, waste disposal services, towing and wrecking services distributors, and hearses. (IR 44 at 5.)

§ 42-1305.[5] Through the issuance of sales tax licenses, the Taxing Authorities monitor the number of active entities that are subject to the tax. For fiscal year 1991-1992, Arizona issued 146,981 sales tax licenses, the City of Phoenix issued 41,392, and the Town of Clifton issued ninety-six. (IR 44.)

Arizona collected $1,941,866,013 in sales and use taxes for the fiscal year ended July 30, 1992. (*Id.*) Santa Fe and Southern Pacific – by any objective measure the two largest railroads in Arizona (IR 1) – pay approximately $600,000 per year in sales taxes. (IR 44.) Railroads operating in Arizona pay only a minimal amount of use tax to the Taxing Authorities.

Because Petitioner did not intervene in the action below until after the original parties had conducted discovery and had begun the process of moving for summary judgment, the record contains little information regarding the amount of taxes that Petitioner has paid. Arizona has audited Petitioner's business and has determined that over a four-year period, Petitioner paid about $50,000 per year in sales taxes, the bulk of which was reported in the amusement classification for receipts from its recreational train rides. Thus, contrary to the Petition's general theme, most of Petitioner's Arizona business activity has nothing to do with competing with motor carriers for freight.

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[5] Almost all Arizona cities and towns have adopted the Model City Tax Code, which imposes a sales tax on virtually the same business activities as the State sales tax, including transportation. Model City Tax Code § 475(d)(1).

Motor carriers, in addition to paying other taxes and fees,[6] are subject to an in-lieu tax called the Motor Carrier Tax. A.R.S. §§ 28-1599 to -1599.46. This tax is calculated based on the distance that a motor carrier has traveled within Arizona and imposed at rates that increase with vehicle weight. A.R.S. § 28-1599.05. Motor carriers also pay a use fuel tax of eighteen cents per gallon. A.R.S. § 28-1501. By comparison, the railroads pay a use tax of only three cents per gallon for the same fuel. (IR 28 at 15.)

Even though Arizona is not constitutionally required to do so, the State limits its sales tax under the transporting classification to intrastate activities only. *See* A.R.S. § 42-1310.02(A) (providing that the tax applies to transporting "from one point to another point in this state"). Thus, railroads do not pay any sales taxes on their interstate operations. By contrast, the taxes that motor carriers pay on the distance that they travel are not similarly limited. The Motor Carrier Tax is imposed on the motor carrier *irrespective* of whether the carrier's journey is in inter- or intra-state commerce.

The Petition's "Factual Background" contains several insufficient, unsupported, or simply argumentative statements. For example, Petitioner alleges that the sales tax is imposed on "the business of transporting for hire persons, freight or property by . . . railroad." Pet. at 1. While this statement is reflective of the wording of the statute, it neglects to inform the reader that less than one percent of

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[6] Motor carriers pay a gross weight fee (A.R.S. § 28-206), plus an Additional Highway Use Tax. A.R.S. § 28-226.

all revenues that the railroads generate by operations within Arizona are subject to the sales tax.[7]

Additionally, Petitioner asserts without citation that "heavy commercial trucks have historically paid to the state less than the full cost of highway maintenance and construction resulting from the motor carriers' use of the roads." Pet. at 2. This alleged fact presumably is based upon a highway study done to measure the imposition of wear and tear upon the state roadway system. Petitioner fails to disclose that the report highlighted that while no group of users pays for all of the wear and tear associated with its use of the roadways, motor carriers pay the most by far. (IR 79 at 4-5.) In any event, the findings in the report are not conclusive by any means.

Petitioner also alleges without citation that "[i]n comparing the cost of shipping goods, shippers of freight must include in their comparison the transaction privilege tax if they ship by rail, but not if they ship by motor carrier." Pet. at 2. This alleged "fact" apparently is

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[7] Indeed, the railroads, unlike most other businesses that pay sales tax, enjoy a special set of statutory tax exemptions that specifically exclude certain of their purchases and activities from taxation. For example, Santa Fe has admitted that 99.17 percent of all revenues that it obtained from trains traveling within Arizona are not subject to the sales tax on transporting because those trains are engaged in interstate commerce. (IR 28 at 12.) Further, Southern Pacific purchased $66,078,001 and $73,110,532 in rolling stock, rails, ties and signal control equipment for calendar years 1990 and 1991, respectively, which it intended to use within Arizona. (IR 28 at 7.) These purchases were exempt from both the sales and the use taxes. A.R.S. §§ 42-1310.01(B)(8), 42-1409(B)(8).

derived from a railroad employee's affidavit that contains improper legal conclusions.

REASONS TO DENY THE PETITION

No compelling reason exists for this Court to review the Ninth Circuit's opinion. First, no novel federal question exists because the Ninth Circuit simply and squarely applied this Court's holding in *Department of Revenue v. ACF Industries, Inc.*, 510 U.S. 332 (1994), to the facts of this case. Second, no conflict exists among the circuits because the three other circuits that have addressed challenges to state taxing statutes under 49 U.S.C. § 11503(b)(4) after *ACF* – the Seventh, Eighth, and Tenth Circuits – have applied the same analysis as the Ninth Circuit did. Third, the alleged conflict among other lower courts does not exist because the cases on which Petitioner relies were all decided before – and are irreconcilable with – this Court's decision in *ACF*, and, in any event, the Petitioner's proffered "competitive disadvantage" test is analytically unsound.

1. The Court of Appeals Correctly Applied This Court's Holding in *Department of Revenue v. ACF Industries, Inc.*

The Ninth Circuit properly applied this Court's holding in *ACF* that

> a State may grant exemptions from a generally applicable ad valorem property tax without exposing the taxation of railroad property to invalidation under subsection (b)(4).

Pet. App. at 11 (quoting *ACF*, 114 S. Ct. at 848).

In *ACF*, this Court analyzed a challenge under 49 U.S.C. § 11503(b)(4) to Oregon's imposition of personal property tax on railroads. The Court meticulously examined the statutory framework within which subsection (b)(4) is found and concluded that it was Congress' desire, as expressed in the literal language of the statute, to allow States to enact exemptions from general taxation schemes as long as the tax that they imposed remained one of "general applicability."

The Court gave three reasons why a State could grant exemptions from generally applicable taxes without subjecting its taxation of railroads to challenge under subsection (b)(4). First, the Court recognized that railroads cannot challenge property tax exemptions under subsections (b)(1)-(3) because exempt property is not part of the comparison class against which discrimination is measured under those subsections. The Court explained that "[i]t would be illogical to conclude that Congress, having allowed the States to grant property tax exemptions in subsections (b)(1)-(3), would turn around and nullify its own choice in subsection (b)(4)." 114 S. Ct. at 849. The Ninth Circuit cited this analysis as its initial reason for rejecting the railroads' discriminatory exemption argument. *See* Pet. App. at 11 ("First, the discriminatory exemption argument fails because the Supreme Court in *ACF* held that discrimination under the 4-R Act does not arise when exemptions are granted from a generally applicable property tax if the railroads are treated fairly in comparison to other industrial and commercial taxpayers subject to the tax.").

The second reason this Court gave in *ACF* to "reinforce [its] construction of the statute" was that Congress

had not spoken with any degree of particularity to the relationship between tax exemptions and subsection (b)(4), and the Court was "confident that [Congress] would have spoken with clarity and precision" if it had intended to restrict state power in this regard. 114 S. Ct. at 850. In applying that analysis, the Ninth Circuit again used nearly identical language: "Accordingly, if Congress, as a condition of permitting state taxation of the railroads through sales and use taxes had intended to restrict state power to exempt other types of businesses from these taxes, Congress would have done so explicitly." Pet. App. at 12.

Finally, in reviewing the other three subsections of § 11503(b), this Court determined that Congress meant to find that discrimination existed when the railroads were treated differently than most, not all, other commercial and industrial businesses. The Court concluded that as long as the railroads were not "either alone or as part of some isolated and targeted group . . . the only commercial entities subject to an ad valorem property tax," the tax should be sustained. *ACF*, 114 S. Ct. at 851. The Ninth Circuit, applying this reason, found no discrimination. *See* Pet. App. at 14.

This Court has provided a bright-line test. The Ninth Circuit applied that test and determined that the Taxing Authorities' sales and use taxes were taxes of general applicability that did not place the railroads in an isolated and targeted group of taxpayers. The court of appeals correctly found that Arizona's taxation scheme effectuated Congress' intent of insuring that railroads are "accorded equal tax treatment with other taxpayers"

because the railroads pay the same sales and use taxes as 146,000 other businesses in Arizona. Pet. App. at 10.

2. No Conflict Exists Between the Decision Below and the Decisions of All the Other Circuit Courts That Have Addressed This Issue.

The Seventh, Eighth, and Tenth Circuit Courts of Appeal have applied the rule that this Court enunciated in *ACF* in the same manner as the Ninth Circuit did to resolve challenges under subsection (b)(4). *See Burlington N. R.R. v. Wisconsin Dep't of Revenue*, 59 F.3d 55 (7th Cir. 1995); *Burlington N. R.R. v. Bair*, 60 F.3d 410 (8th Cir. 1995), *cert. denied*, 116 S. Ct. 914 (1996) ("*Bair*"); *Burlington N. R.R. v. Huddleston*, 94 F.3d 1413 (10th Cir. 1996). Importantly, while the circuit courts have all applied this Court's rule consistently, the different facts presented in those cases have produced different ultimate results, thus proving that this Court developed a reasonable and workable test.

In *Wisconsin Department of Revenue*, the Seventh Circuit upheld Wisconsin's personal property tax scheme. The parties had stipulated that over eighty percent of the personal property possibly subject to taxation in Wisconsin was exempted by law. The court observed that the "Supreme Court held [in *ACF*] that a state's exemptions of various classes of non-railroad property from a generally applicable *ad valorem* property tax are not cognizable" under subsection (b)(4). 59 F.3d at 55-56. The court then held that "[t]he railroads can only succeed by showing that the actual tax levied is a general tax in name only and is in fact a tax on railroads. The only number relevant

to that inquiry is the percentage of the total tax levy that falls on railroads." *Id.* at 58. Here, as in the Seventh Circuit case, the railroads pay an incredibly insignificant amount of the over $1.9 billion in sales and use tax collected annually by the Taxing Authorities.

In *Bair*, the Eighth Circuit struck down an Iowa law that provided for the imposition of a personal property tax upon railroads and other select taxpayers. The court observed that Iowa itself does not have a general personal property tax; rather, the personal property of the railroads and certain utilities are included in the valuation of real property and assessed at real property rates. The court held that the tax was not "generally applicable" because Iowa did not have a tax from which it granted exemptions, only a tax that had "singled out for taxation all the personal property of railroads and a handful of interstate utilities, while leaving untaxed most of the personal property of every kind." 60 F.3d at 413. The court recognized the bright line "general applicability" test derived from *ACF* as the Seventh Circuit had. The Ninth Circuit applied the same test here and concluded that the Taxing Authorities' sales and use taxes were taxes of general applicability that applied to over 146,000 state taxpayers.

In *Huddleston*, the Tenth Circuit struck down a Colorado statute that provided for taxation of personal property, but exempted intangible personal property. The exemption, however, did not extend to railroads or certain other public utilities. The court held that the tax was not "generally applicable" because the "tax exemption applie[d] to *all* commercial and industrial taxpayers other

than 'public utilities.' " 94 F.3d at 1417 (emphasis in original). The court noted that a truly nondiscriminatory tax would be one that treated railroads like "other commercial and industrial taxpayers." *Id.* (*citing ACF, McNamara,* and the Ninth Circuit's decision in this case). In *Huddleston,* the court concluded that while most other industrial and commercial taxpayers did not pay the tax, railroads did.

Because the Seventh, Eighth, Ninth, and Tenth Circuits have all consistently applied *ACF's* clear bright-line "general applicability" rule, there is no reason for this Court to revisit that rule.

3. The Other Lower Court Cases Petitioner Relies Upon Were Decided Before *ACF* and Used an Improper Test.

Petitioner's challenge is predicated upon the premise that in enacting the 4-R Act, Congress intended to ensure a nationwide tax policy in which the tax rate of railroads would never be greater than that of their competitors. Under Petitioner's test, the taxation of railroads must be compared to the taxation of those who compete with the railroads for freight traffic. Petitioner's argument fails because all of Petitioner's case authority predates *ACF* and is inconsistent with *ACF's* express holding. Petitioner's proffered test also is inconsistent with the express language of the 4-R Act, which completely removes other transporters from any comparative taxation equations. Moreover, none of Petitioner's cases actually focused on the language of the statute itself, and all of them therefore used the wrong test.

a. The cases that Petitioner relies upon all pre-date *ACF* and are incorrect under the rule that *ACF* established.

Petitioner bases its entire legal challenge upon one district court and two state court opinions issued before this Court's decision in *ACF*.[8] These decisions have no precedential effect because they cannot be reconciled with this Court's decision in *ACF*. Petitioner makes no effort to discuss the effect that *ACF's* "general applicability" test would have upon the result in the three cases. Likewise, Petitioner does not attempt to distinguish the test's application to the facts of this case. Petitioner instead asserts that:

> The majority opinion below misapplied this Court's *ACF Industries* holding to validate the imposition of a nonproperty tax scheme which exempts the railroad's principal competitor.

Pet. at 4. This argument ignores *ACF's* important lesson that "§ 11503, which expresses Congress' resolution of the matter, does not limit the States' discretion to exempt nonrailroad property, but not railroad property, from *ad valorem* property taxes of general application." *ACF*, 114 S. Ct. at 852. While Petitioner may argue for a different test for identifying discrimination, Congress has not chosen to recognize discrimination in every situation in which railroads are treated differently than someone else. Petitioner has failed to identify anything in the 4-R Act's

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[8] *See Atchison, Topeka and Santa Fe Ry. v. Bair*, 338 N.W.2d 338 (Iowa 1983) ("*Bair-II*"); *Burlington N. R.R. v. Triplett*, 682 F. Supp. 443 (D. Minn. 1988); and *Burlington N. R.R. v. Commissioner of Revenue*, 509 N.W.2d 551 (Minn. 1993).

legislative history to establish that Congress considered the taxation of railroads' competitors in creating the Act. More directly, Congress did not enact a statute that required the type of competitor equality that Petitioner seeks. What Congress required is that States must treat railroads the same as they treat a large group of other State taxpayers. As the Ninth Circuit observed:

> The only simple way to prevent tax discrimination against the railroads is to tie their tax fate to the fate of a large and local group of taxpayers.

Pet. App. at 9-10 (*quoting McNamara*, 817 F.2d at 375). Congress sought general equality, not equality measured against one particular group or industry.

b. The three decisions themselves do not have a strong foundation.

The *Bair-II*, *Triplett*, and *Commissioner of Revenue* decisions lack a solid foundation. Although *Bair-II* essentially applied the competitive disadvantage test, no majority favored adopting that test. The single concurring Iowa justice in the 4-1-4 split decision stated that "competitive disadvantage is not a practical standard by which to determine whether a tax is discriminatory. Too many variables are involved to make such comparisons meaningful." *Bair-II*, 338 N.W.2d at 348.[9]

[9] Although the *Bair-II* court used the wrong test, it probably reached the correct result on the merits due to the extreme factual circumstances involved in that case. In *Bair-II*, the Iowa General Assembly enacted a special excise tax on railroads measured by the amount of fuel consumed to propel railway

In the thirteen years since *Bair-II* was decided using the competitive disadvantage test, only two courts – both in Minnesota – have applied that test. The *Triplett* decision is devoid of legal analysis and simply defers to *Bair-II*. The *Commissioner of Revenue* decision, while containing additional analysis, also relies upon the *Bair-II* and *Triplett* decisions. The inconsistency with the holding of these three cases and *ACF* is that the three courts, in applying the competitive disadvantage test, failed to recognize that Congress meant only to place railroads in a position where they would not be singled out for taxation; Congress did not intend to put railroads in a "most favored taxpayer" status. This Court in *ACF* recognized that the railroads could be subject to a tax that exempted various others as long as, overall, the tax was one of general applicability and the railroads were not being singled out for disproportionate taxation.

Congress only meant to require the States to treat the railroads the same as most other industrial and commercial taxpayers in the State, not to give them a preference. *See Ogilvie v. State Bd. of Equalization*, 657 F.2d 204 (8th Cir. 1981); *CSX Transp., Inc. v. Tennessee Bd. of Equalization*, 801 F. Supp. 28 (M.D. Tenn. 1992). Railroads still must "pay their fair share of state taxes." *McNamara*, 817 F.2d at 378.

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vehicles in the State. *Id.* at 341. That tax applied only to the railroads and was therefore easily attacked by the railroads.

c. The plain language of the statute evidences Congress' intent that the taxation of competitors not factor into the discrimination equation.

The most convincing reason to reject the Petitioner's proposed "competitive disadvantage" test in determining discrimination is the language of the 4-R Act itself.[10] The the 4-R Act defines the term "commercial and industrial property," the class that Congress specifically chose to compare the taxation of railroad property to in 49 U.S.C. § 11503(b)(1)-(3), as "property, **other than transportation property** and land used primarily for agricultural purposes or timber growing, devoted to a commercial or

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[10] 49 U.S.C. § 11503 provides as follows:

> (b) The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision may not do any of them:
>
> (1) assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
>
> (2) levy or collect a tax on an assessment that may not be made under clause (1) of this subsection.
>
> (3) levy or collect an ad valorem tax on rail transportation property at a tax rate that exceeds the tax rate applicable to the commercial and industrial property in the same assessment jurisdiction.
>
> (4) impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the [Interstate Commerce Commission].

industrial use and subject to a property tax levy." 49 U.S.C. § 11503(a)(4) (emphasis added). Thus, a property tax that taxed the railroads and not other transporters would be non-discriminatory under the 4-R Act by the express wording of the statute. Indeed, the express language of the 4-R Act specifically permits differentiation in the taxation of railroad property and other "transportation property" and refutes the use of the competitive disadvantage test. The three decisions Petitioner relies upon never focused upon the words of the statute allowing for this differentiation in taxation among those with transportation property.

The 4-R Act provides for comparison of the taxation of railroads property with that of other "commercial and industrial property," not just the property of railroads' competitors. In fact, Congress defined the class to which railroads may be compared and specifically excluded the railroads' competitors when determining if rate and ratio discrimination existed. It would be illogical for Congress, having allowed for differentiation in taxation between railroads and their competitors in subsections (b)(1)-(3), to nullify its own choice in subsection (b)(4) to ban such difference.[11] Under the express terms of the 4-R Act, there

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[11] This Court rejected a similar argument in *ACF*:

> It would be illogical to conclude that Congress, having allowed the States to grant property tax exemptions in subsections (b)(1)-(3), would turn around and nullify its own choice in subsection (b)(4). So the Carlines' reading of subsection (b)(4), while plausible when viewed in isolation . . . is untenable in light of § 11503 as a whole.

ACF, 114 S. Ct. at 849.

would be no legally cognizable discrimination even if the railroads were subject to the tax and their competitors were not.

d. The Ninth Circuit correctly found no discrimination because Petitioner was taxed the same as other industrial and commercial taxpayers.

Subsection (b)(4) prohibits a tax that "discriminates against a rail carrier." The Court in *ACF* began its analysis with the question of who the railroads should be compared with in determining if discrimination exists. The Court found that the proper comparative class is commercial and industrial taxpayers in general, and the same conclusion applies here. If the comparison were only between railroads and motor carriers, any "discrimination" could be avoided entirely by taxing both at a rate higher than other commercial or industrial taxpayers. Thus, not only is Petitioner's narrow comparative class argument wrong, but it also ignores the actual unintended consequences that could occur from such a comparison.

Referring to other portions of the 4-R Act (specifically, subsections (b)(1) - (3)), the Court noted that Congress specifically made reference to a comparative class, stating that the comparison was the assessment rate and ratios for the railroads' property against those owned by other commercial and industrial taxpayers. *ACF*, 114 S. Ct. at 848. Subsection (b)(4) is silent as to comparative class. Because Congress chose to analyze the railroads'

tax responsibilities against the broad class of all industrial and commercial taxpayers in the first three subsections of the statute, logic dictates that the same standard be applied in subsection (b)(4).

Two other circuits, in analyzing the propriety of non-property tax challenges under subsection (b)(4), have used this test when comparing the railroads to other industrial and commercial taxpayers. The Fifth Circuit stated:

> We think the best course is to require that the railroads be taxed only under taxes applicable to "other commercial and industrial" taxpayers.

McNamara, 817 F.2d at 375. Similarly, the Seventh Circuit noted:

> By analogy we may assume that a tax is "discriminatory" within the meaning of the fourth subsection if it imposes a proportionately heavier tax on railroading than on other activities. . . .

Burlington N. R.R. v. City of Superior, 932 F.2d 1185, 1187 (7th Cir. 1991). In a property tax case, the Tenth Circuit similarly observed:

> Both subsection (1)(a) and (1)(c) of § 306 establish a comparison class of "commercial and industrial property," and we can think of no sound reason why Congress did not intend the same class to be used in analyzing discrimination under subsection (1)(d).

Huddleston, 94 F.3d at 1417.

Here, the sales and use taxes are generally applicable to more than 146,000 industrial and commercial taxpayers

within the Taxing Authorities' jurisdictions. The proper comparative class for testing discrimination is all other commercial and industrial taxpayers subject to the taxes, and the Fifth, Seventh, Ninth and Tenth Circuits have consistently applied this principle.

* * *

There is no compelling reason for this Court to grant a writ of certiorari. The Ninth Circuit properly applied this Court's recent ruling in *ACF* on the exact statute at issue. No conflict exists between the decision of the Ninth Circuit and the decisions reached by several other circuit courts. The Ninth Circuit, as have the other circuits to decide cases after this Court's decision in *ACF*, applied this Court's clear holding in *ACF* to a case brought under 49 U.S.C. § 11503(b)(4), and under that holding, the Taxing Authorities should prevail.

CONCLUSION

This Court should deny the petition for a writ of certiorari.

Respectfully submitted,

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November 8, 1996

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